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Statement of Senator Hart opening hearings of Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary on S. 2507 and S. 2321, 90th Cong., 1st Sess. (1967) 14

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IN THE

Supreme Court of the United States

October Term, 1970

No.

ARTURO FORNARIS, JR.,

Appellant,

v.

THE RIDGE TOOL CO., *et al.*,

and

THE COMMONWEALTH OF PUERTO RICO,

Appellees.

On Appeal from the United States Court of Appeals for the First Circuit

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JURISDICTIONAL STATEMENT

JURISDICTIONAL STATEMENT

The appellant, Arturo Fornaris, Jr., appeals from the judgment entered on March 17, 1970, in this proceeding by the United States Court of Appeals for the First Circuit, pursuant to 28 U.S.C. § 1254(2).

OPINION BELOW

The opinion of the First Circuit, rendered on March 17, 1970, is reported at 423 F.2d 563 and is reprinted in the Appendix hereto, p. 31, *infra*.

The United States District Court for the District of Puerto Rico on August 11, 1969, entered a Memorandum and Order denying a motion to dismiss on constitutional grounds and certifying that the order involved a controlling question of law as to which there are substantial grounds for difference of opinion and that an immediate appeal from the order might materially advance the ultimate termination of the litigation. That order, which is unreported, is reprinted in the Appendix hereto, p. 45, *infra*, including an opinion by the Superior Court of Puerto Rico, San Juan Part, in *Construction Machinery & Supplies Corp. v. Construction Machinery Co.*, that was attached to that order.

JURISDICTION

The judgment of the Court of Appeals, acting on an interlocutory appeal allowed pursuant to 28 U.S.C. §1292(b), was entered on March 17, 1970. The appellant duly filed in the Court of Appeals on May 4, 1970, a notice of appeal that is reproduced in the Appendix hereto, p. 44, *infra*. On June 3, 1970, Mr. Justice Brennan signed an order extending the time for docketing this appeal to and including August 14, 1970.

The appeal jurisdiction of this Court is invoked under 28 U.S.C. §1254(2); should the Court determine that the appeal has been improvidently taken, appellant requests that this jurisdictional statement be treated as a petition for certiorari, as 28 U.S.C. §2103 requires, and that this Court's certiorari jurisdiction under 28 U.S.C. §1254(1) be invoked. The jurisdictional problem as to the appeal is treated more fully herein under the heading "The Question of Jurisdiction," p. 10, *infra*.

QUESTIONS INVOLVED

1. Whether the Contract Clause of the United States Constitution, Article I, Section 10, or the so-called retrospective aspects thereof, is incorporated by reference into the Due Process Clause either of the Fifth Amendment or of the Fourteenth Amendment.

2. Whether the Puerto Rican Dealer's Act, 10 L.P.R.A. §278 et seq., as construed to give a damage action for a termination without just cause of a franchise agreement permitting termination at will, violates the Contract Clause of the United States Constitution or the Due Process Clause either of the Fifth Amendment or of the Fourteenth Amendment.

3. Whether a federal court should abstain from adjudicating the validity of a Puerto Rican statute in light of the United States Constitution where (a) there has been no authoritative interpretation or evaluation of the statute by the Supreme Court of Puerto Rico, and (b) the factual development in the particular case before the court is insufficient to permit a determination of precisely what portions of the statute are applicable and precisely what constitutional rules should be applied to the facts.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

United States Constitution:

> Article I, Section 10: "No State shall . . . pass any . . . Law impairing the Obligation of Contracts . . ."
>
> Amendment V: ". . . nor shall any person . . . be deprived of life, liberty, or property, without due process of law . . ."

Amendment XIV, Section 1: " . . . nor shall any State deprive any person of life, liberty, or property, without due process of law . . ."

Puerto Rican Dealers' Contract Law, 10 L.P.R.A. § 278, et seq.:

This statute is reprinted in the Appendix hereto, p. 62, *infra*, in its amended form; the changes from the original form are indicated in the statements following each section. The decision below tested the statute in its original form, but the changes effected in 1966 are not material to the decision.

STATEMENT OF THE CASE

Arturo Fornaris, Jr., the appellant herein, initiated this proceeding on September 23, 1966, by filing a complaint in the Superior Court of Puerto Rico, San Juan Part, seeking the recovery of damages in the amount of $175,000, plus attorneys' fees, from the appellee Ridge Tool Company. Fornaris, a citizen of Puerto Rico, alleged that for more than 29 years he had been the exclusive distributor in Puerto Rico of merchandise manufactured by the Ridge Tool Company, which is an Ohio corporation.[1] The distributorship contract was cancelled or terminated, effective April 15, 1966, by the Ridge Tool Company.

The complaint alleged that such termination was "without just cause" and that the "manifest purpose" was to permit the Ridge Tool Company to sell its merchandise in Puerto Rico "taking advantage of the market that the plaintiff [Fornaris] has created in the

[1] Also named as a defendant was the Ridge Tool International Co., Inc., a subsidiary of the Ridge Tool Company in charge of foreign sales and the export market. The Ridge Tool International Co., Inc., is also an appellee before this Court.

country through years of effort and perseverance and depriving him of the just and due compensation to which he has a right under the law, and to procure for himself large economic benefits." It was further asserted that the Ridge Tool Company had "acted jashly and with obvious and manifest scorn of the law of Puerto Rico" inasmuch as the appellant had warned the company that the termination was "illegal in Puerto Rico" and "gives right to indemnification for the damages caused."

In October of 1966 the Ridge Tool Company caused the case to be removed to the United States District Court for the District of Puerto Rico, invoking the diversity jurisdiction of that court. The company thereupon filed a motion to dismiss the action. The motion asserted that Fornaris' claim "is based upon, and is made in reliance upon the provisions of Law Number 75, of June 24, 1964, as amended, (10 LPRA 278 et seq.), hereinafter referred to as the 'Dealer's Act'." The motion then alleged that the Dealer's Act is "void and unconstitutional"

> "... because it is an arbitrary exercise of the police power of the Commonwealth of Puerto Rico; because it cannot be applied to existing contracts ...; because it violates due process of law in that it sets up vague, indefinite and uncertain standards so that men of common intelligence must guess as to its meaning; because it violates equal protection of the laws since it is class legislation protecting existing dealers only, and denies to newcomers the opportunity to contract or attempt to contract with manufacturers in Puerto Rico; because it denies freedom of contract; because it forces violations of Federal and local anti-trust legislation; because it imposes burdens upon manufacturers who are using distributors in Puerto Rico on the date of the adoption of the law and its various amendments not imposed on

other manufacturers who distribute directly in Puerto Rico through their own employees; and because the law contains no requirement that the parties act in good faith with the consuming public."

The Commonwealth of Puerto Rico was allowed to intervene in the case solely to defend the constitutionality of the Puerto Rican statute at stake, the Dealer's Act. Thereafter, in March of 1968, the District Court entered an order staying further proceedings until determination of an appeal then pending before the First Circuit, *United Medical Equipment Corp. v. S. Blickman, Inc.*, No. 6876, wherein the constitutionality of the Dealer's Act was being challenged on the same grounds as those raised herein by the Ridge tool Company's motion to dismiss.[2] But that appeal was mooted by settlement of the case after oral argument but before completion of the First Circuit's opinion.

Similar constitutional claims respecting the Puerto Rican statute were involved in an effort to secure an interlocutory appeal by the First Circuit in *Carmac Chemical Corp. v. Application Engineering Corp.*, No. 7177. The First Circuit had deferred consideration of the application for leave to appeal pending receipt of the views and decision of at least the Superior Court of Puerto Rico with respect to the constitutionality of the Puerto Rican Dealer's Act. But the *Carmac* case, like the *United Medical Equipment* case, was settled before any decision by the First Circuit could be rendered.

In December of 1968 the Superior Court of Puerto Rico determined that the Puerto Rican Dealer's Act

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[2] The District Court for the District of Puerto Rico had ruled that, while the 1966 amendment to the Dealer's Act was prospective only, there was no merit to the allegation that the Act is an arbitrary exercise of the police power of the Commonwealth of Puerto Rico. *United Medical Equipment Corp. v. S. Blickman, Inc.*, 260 F. Supp. 912, 913 (D.P.R. 1966).

violated neither the United States Constitution nor the Puerto Rican Constitution. *Construction Machinery & Supplies Corp. v. Construction Machinery Co.*, Civil No. 67-3549. As respects the United States Constitution, the court held that the Act did not contravene the Contract Clause, the Due Process Clause or the Equal Protection Clause. A translation of that court's opinion was attached to the Memorandum and Order of the District Court in the instant case and appears in the Appendix hereto, p. 45, *infra*. This opinion of the San Juan Section of the Superior Court, however, is not considered under Puerto Rican law to be authoritative or binding on other courts.

As a result of these two abortive appeals, the District Court herein ordered a hearing on the motion to dismiss. At this juncture, no answer had been filed and no evidence taken or facts conceded with respect to the allegations of the complaint. The possible non-constitutional defenses were unknown. Following that hearing the court on August 11, 1969, entered its Memorandum and Order denying the motion to dismiss on constitutional grounds. See Appendix hereto, p. 45, *infra*. The court based its denial on its "prior decision in this area," *Ruiz v. Economics Laboratory, Inc.*, 274 F. Supp. 14 (D.P.R. 1967),[3] and on the recently rendered decision of the Puerto Rican Superior Court in *Construction Machinery & Supplies Corp. v. Construction Machinery Co.*, a copy of which was attached to the order. The court also included in its order a statement, in conformity with 28 U.S.C. §1292(b), that the order dismissing the constitutional defense of the Ridge Tool Company "involves a controlling question of law as to which there is substantial

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[3] An effort to secure an interlocutory appeal of the order in the *Ruiz* case was unsuccessful; the First Circuit denied the petition for permission to appeal the interlocutory order because of the then pendency of the appeal in the *United Medical Equipment* case, which was later settled and withdrawn.

ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation."

In petitioning the First Circuit for permission to appeal from the District Court's interlocutory order, the Ridge Tool Company stated that the controlling question of law sought to be presented "is whether Act No. 75 of 1964, as amended, the sole basis for plaintiff's claim, (*Francisco Garraton v. Kimberly Clark Corp.*, 267 F. Supp. 909 (D.C.P.R. 1967) is valid and enforceable." And it was further stated that among the challenges to the constitutionality of the statute was the claim that the Dealer's Act "denies to defendant and other manufacturers and/or grantors Due Process of Law as guaranteed by the Constitution of the United States in that it is vague, unreasonable, arbitrary or capricious." References were also made to the claims that the Act was "class legislation violative of the Equal Protection Clause" and that the Act "may not be applied to affect contracts executed prior to June 24, 1964."

The First Circuit allowed this petition to permit an interlocutory appeal. But it ordered that the appeal be treated as submitted without oral argument, which had not been requested, "in view of the extensive argument that was heard in *United Medical Equipment Corp. v. S. Blickman, Inc.*, No. 6876, but the court will consider all briefs filed in that case as being filed herein." Thus the court had the advantage of the many briefs, including numerous *amicus* briefs filed in response to a general invitation, that had been submitted in the *United Medical Equipment* case, which had been mooted by settlement prior to decision. The instant parties, including the Commonwealth of Puerto Rico, were afforded the opportunity to file additional briefs.

Among the points raised and discussed in the briefs in the *United Medical Equipment* case, and thus incorporated by reference in the instant appeal, was the

contention that the unique status of the Commonwealth of Puerto Rico under its compact with the Congress of the United States made the doctrine of abstention peculiarly appropriate in a situation involving the construction and validity of a Puerto Rican statute. It was urged that a federal court should abstain from construing such a statute and testing its constitutionality until the Supreme Court of Puerto Rico has had an opportunity to interpret the statute and to assess its validity under the Puerto Rican Constitution as well as under the United States Constitution.[4] This contention was reiterated by the appellant Fornaris in his motion for reconsideration of the District Court's order certifying the appropriateness of an interlocutory appeal. But the First Circuit's opinion in this case did not mention or resolve the abstention claim, although it did acknowledge that "we have the benefit of the opinion of the Puerto Rico Superior Court in *Construction Mach. & Supplies Corp. v. Construction Mach. Co.*, decided December 23, 1968, upholding the act's consitutionality." See p. 33, *infra*. But that decision was only that of the San Juan Section of the Superior Court.

The First Circuit vacated the judgment of the District Court and directed that judgment be entered in favor of the appellee Ridge Tool Company. This action was premised solely on the court's determination that the Puerto Rican Dealer's Act, in its original and unamended form, is violative of "the due process clause of the federal constitution" by virtue of its retroactive alteration of contractual relationships. Under the court's view, a pre-statutory franchise contract between a manufacturer and a dealer is converted by the Act from one terminable by either party without cause into one that can be terminated by the manufacturer only for "just

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[4] Such a contention was advanced in the *United Medical Equipment* case in the Brief for Amici Curiae La Electronica, Inc., and Wallace Torres Canet, pp. 28-30.

cause." Such a conversion was said to force the manufacturer to adopt "heavy contractual obligations that it never assumed," whereas a dealer "could have no legitimate expectation of non-terminable contracts."

In concluding that this change in property rights was so drastic in nature as to contravene due process concepts, the First Circuit did not specify whether it was the Due Process Clause of the Fifth Amendment or that of the Fourteenth Amendment that was involved. The court merely stated that it had "no thought that Puerto Rico is in a more favored position in this respect than is a state or the federal government," pp. 37-38, *infra*, and referred to an earlier opinion of its own, *Mora v. Mejias*, 206 F.2d 377, 382 (1st Cir. 1953), proclaiming that "the important point is that there cannot exist under the American flag any governmental authority untrammeled by the requirements of due process of law as guaranteed by the Constitution of the United States." And while the First Circuit relied upon cases arising under the constitutional prohibition against impairing the obligation of contracts, the court did not rest its decision upon the Contract Clause inasmuch as "the due process clause of the federal constitution provides essentially the same restraint so far as retrospectivity is concerned." See p. 37, *infra*.

THE QUESTION OF JURISDICTION

The appellant has invoked this Court's appeal jurisdiction under 28 U.S.C. §1254(2), which provides that cases in the United States courts of appeals may be reviewed by this Court

> "By appeal by a party relying on a State statute held by a court of appeals to be invalid as repugnant to the Constitution, treaties or laws of the United States, but such appeal shall preclude review by writ of certiorari at the instance of such appellant, and the review on appeal shall be restricted to the Federal questions presented."

In this case the appellant has relied upon a Puerto Rican statute that the First Circuit has held to be invalid as repugnant to the Due Process Clause of either the Fifth Amendment or of the Fourteenth Amendment of the Constitution of the United States. The obvious question that arises is whether a Puerto Rican statute is a "State statute" within the meaning of §1254(2).

While there is no definitive ruling by the Court on this question, appellant submits that every relevant consideration leads to the conclusion that a Puerto Rican statute is a state statute in the §1254(2) sense and that an appeal properly lies in this instance. Puerto Rico is not a state, constitutionally speaking. But the judicial and legislative characteristics of its autonomous commonwealth status, combined with the applicability to Puerto Rico of at least the due process provisions of the United States Constitution,[5] have led to the treatment of Puerto Rico as the equivalent of a state for jurisdictional purposes in this Court. No exception is apparent as to §1254(2).

To begin with, Congress has provided in 28 U.S.C. §1258 for the review by this Court of final judgments of the Supreme Court of Puerto Rico.[6] It has specified, in

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[5] "The question of what U.S. Constitutional provisions apply to Puerto Rico is unclear. . . .The constitutional restrictions upon a State of the Union with respect to the regulation of interstate and foreign commerce (Art. I, sec. 8, clause 3) and prohibitions upon the levying of duties or imposts upon imports (Art. I, sec. 10, clause 2) were held not to apply to Puerto Rico prior to Public Law 600 (64 Stat. 319, 48 USC Sections 731b-731e). Due process is the only constitutional requirement specifically held to be applicable to Puerto Rico, although whether it is the 5th or 14th amendment is not clear." Report of the United States–Puerto Rico Commission on the Status of Puerto Rico, pp. 44-45 (Aug. 1966).

[6] Section 1258 was enacted in 1961. For review purposes, the statute accords to the Puerto Rico Supreme Court the status of the highest court of a state and was deemed to be "appropriate in view of the change in the status of Puerto Rico from that of a territory to that of an associated commonwealth under the Act of Congress." H. Rep. No. 683, 87th Cong., 1st Sess., p. 2 (1961).

language identical to that used in §1257 as to the review of judgments of the highest courts of states. The types of judgments of the Puerto Rican court that may be reviewed by appeal and by certiorari. Thus an appeal lies under §1258 (2) where the judgment is in favor of the validity of a Puerto Rican statute in light of the United States Constitution.

Soon after the enactment of §1258 this Court promulgated Rule 61, which provides that

> "The term 'state court' when used in these rules includes the Supreme Court of the Commonwealth of Puerto Rico, and references in these rules to the law and statutes of a state include the law and statutes of the Commonwealth of Puerto Rico."

This provision reflects a general jurisdictional treatment by this Court of Puerto Rican courts and Puerto Rican statutes as the equivalents of state courts and state statutes. While the main purpose of Rule 61 undoubtedly was to implement §1258, Rule 61 also serves generally to give a Puerto Rican content to the phrase "statutes of a state." Thus when Rule 15(1)(v) speaks of the involvement for appeal purposes of "the validity of the statute of a state," Rule 61 encompasses within that phrase a Puerto Rican statute. And since Rule 15 (1) (v) is obviously applicable to appeals other than those arising under §1258(2), the Puerto Rican inclusion has relevance wherever an appeal can be said to involve "the validity of the statute of a state."

The reference in §1254(2) to "a State statute held by a court of appeals to be invalid" under the United States Constitution—a concept identical in nature to the many references to state statutes throughout the Rules of this Court—has in effect been interpreted by this Court's Rule 61 as including the laws and statutes of the Commonwealth of Puerto Rico. To conclude otherwise is

to ascribe to the reference in §1254(2) to "a State statute" a different and more restrictive meaning than that given to it in the Rules of this Court. Indeed, in view of the effort by Congress in §1258 to equate Puerto Rican courts and statutes with state courts and statutes, no reason is apparent for treating a Puerto Rican statute as other than a state statute when the decision as to its constitutional validity happens to be rendered by the First Circuit rather than by the Puerto Rican Supreme Court. An appeal should thus be considered proper under §1254(2) in this case.

Should the Court be of the view that an appeal is improper under these circumstances, appellant requests that the Court exercise its power under 28 U.S.C. §2103 to treat this jurisdictional statement as a petition for writ of certiorari and to take appropriate action on that basis. See *El Paso v. Simmons*, 379 U.S. 497, 501-503 (1965). As explained in the *El Paso* case, this power to treat an improvident appeal as a request for certiorari is in no way diluted by the provision of §1254(2) that an appeal "shall preclude review by writ of certiorari at the instance of the appellant." That provision "means only that if an appeal is proper and has been taken, certiorari will not thereafter be available."

A subsidiary problem of jurisdiction by way of appeal may be present as to the question here raised concerning the obligation of the lower federal courts to abstain from adjudicating the federal constitutional question pending a decision by the Puerto Rican Supreme Court as to the interpretation and scope to be accorded the Dealer's Act in question. Section 1254(2) restricts review on appeal "to the Federal questions presented." While it is not clear whether such reviewable federal questions include only those relating to the validity of the statute or whether they also cover federal questions in the case pertaining to other matters, appellant submits that the abstention problem is so intimately entwined with the propriety of the federal

court's decision invalidating the statute as to be considered a part of or related to the federal constitutional question. If that be true, this Court can clearly consider the abstention problem as a facet of this appeal under §1254(2).

THE QUESTIONS ARE SUBSTANTIAL.

1. The decision below creates novel problems of constitutional power to control the widespread practice of arbitrary cancellation of franchise agreements.

The First Circuit's determination in this case finds no direct or indirect precedent in the decisions of this Court. And that determination has created problems of the first magnitude in both the constitutional and the business-world sense.

Basically at stake here is the power of government—be it the Commonwealth of Puerto Rico, any of the fifty state governments, or even the federal government—to impose civil sanctions on or otherwise control the widespread practice of arbitrary cancellation by manufacturers of franchise dealers' contracts. Franchising itself is a highly significant business practice. It has been estimated that franchising accounts for 10 per cent of the gross national product and 25 per cent of all retail sales; from $70 to $91 billion worth of goods and services are sold annually in the United States through the 400,000 businessmen who are franchisees.[7] But the disparity of economic power as between the franchisor and franchisee is frequently such as to permit the franchisor to insert into the franchise contract the right to terminate at will and without cause. And that arbitrary

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[7] See Report of the Federal Trade Commission Ad Hoc Staff Committee on Franchising, p. 6 (1969); Statement of Senator Hart in opening hearings of the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary on S. 2607 and S. 2321, 90th Cong., 1st Sess., p. 1 (1967).

right has been used by unscrupulous manufacturers to insist upon unreasonable or illegal demands[8] or to cancel the contract outright without regard to the impact on the franchisee's business or the local economy.

Congress was sufficiently concerned about such franchise evils in the automobile industry that in 1956 it enacted the Automobile Dealers' Day in Court Act, 15 U.S.C. §§1221-1225. That act is premised on the Congressional determination "that in the automobile industry concentration of economic power has increased to the degree that traditional contractual concepts are no longer adequate to protect the automobile dealers under their franchises."[9] The Act itself authorizes damage suits by a franchised automobile dealer where the automobile manufacturer has failed to act "in good faith" in "terminating, canceling, or not renewing the franchise with said dealer." 15 U.S.C. §1222.

Since 1937, more than twenty states have enacted legislation designed to eliminate various unfair practices that have been inflicted by automobile manufacturers on franchised dealers.[10] Of those states, at least eight have

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[8]Unreasonable restrictions thereby imposed on the franchisee may have antitrust implications. See, e.g., *United States v. General Motors Corp.*, 384 U.S. 127, 143-144 (1966); *Perma Life Mufflers, Inc. v. International Parts Corp.*, 392 U.S. 134, 139-140 (1968). It has been noted that the "arbitrary or unreasonably oppressive termination of franchises as ancillary to any of the unlawful restraints in connection with franchise agreements aggravates the offensiveness and unlawfulness of such restraints." Report of the Federal Trade Commission Ad Hoc Staff Committee on Franchising, p. 36 (1969).

[9]H. Rep. No. 2850, accompanying S. 3879, 84th Cong., 2d Sess. (July 20, 1956), quoted in 3 U.S. Code Cong. and Admin. News, 84th Cong. 2d Sess., 1956, p. 4597.

[10]See, generally, Kessler, *Automobile Dealer Franchises: Vertical Integration by Contract*, 66 Yale L. J. 1135, 1169 (1957); Brown and Conwill, *Automobile Manufacturer-Dealer Legislation*, 57 Colum. L. Rev. 219 (1957); 7 Am. Jur. 2d, Automobiles and Highway Traffic, §347; 14 Blashfield, Automobile Law and Practice, pp. 341-345 (3rd ed., 1969); Annotation, 7 A.L.R. 3d 1173 (1966).

adopted statutes of a nature substantially similar to the federal proscription against bad faith termination or cancellation of automobile dealer franchise agreements.[11] The terminations which have been outlawed by these states have been variously described in the statutes as "unfair," "without just provocation," "without due regard to the equities of the dealer," and "without just cause," in contrast to the federal statute's concept of acting "in good faith" in terminating a franchise. With

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[11] The eight states that have enacted such legislation are:

1. *Wisconsin*—Wis. Stat. §218.01(3)(a)17 (1967). This statute prohibits an automobile manufacturer from cancelling or failing to renew a franchise "unfairly, without due regard to the equities of the dealer and without just provocation." It has been held on its face "to be a proper exercise of the police power." *Forest Home Dodge, Inc. v. Karng*, 29 Wis. 2d 78, 138 N.W. 2d 214 (1965); *Kuhl Motor Co. v. Ford Motor Co.*, 270 Wis. 488, 71 N.W. 2d 420 (1955).

2. *Minnesota*—Minn. Laws, Ch. 626 (1955). This statute makes it unlawful for any auto manufacturer "to cancel or refuse to renew the franchise. . .without just cause." Its constitutionality has been sustained in *Willys Motors v. Northwest Kaiser-Willys, Inc.*, 142 F. Supp. 469 (D. Minn. 1956).

3. *Iowa*—Iowa Code §322.3 (1966). This statute prohibits an auto manufacturer from terminating or failing to renew any franchise "without just, reasonable and lawful cause." Criminal sanctions are provided.

4. *Florida*—Fla. Stat. Ann. §320.64(8) (1968). Under this statute, an auto manufacturer's license may be denied if it has cancelled a franchise "unfairly or without regard to the equities of a motor vehicle dealer or without just provocation."

5. *North Carolina*—N. C. Gen. Stat. §20-305 (1965). This renders it unlawful for an auto manufacturer "unfairly without due regard to the equities of the dealer, and without just provocation, to cancel the franchise of such dealer."

6. *Rhode Island*—Pub. Laws of R. I., 1950, Ch. 2595, Art. VIII.

7. *New York*—N. Y. Gen. Bus. Law §197 (Supp. 1956). A proposal to amend and expand this law is now pending (proposed Assembly Act No. 739, 1969 Sess.).

8. *Colorado*—The Colorado statute, which used the same language as the North Carolina and Florida statutes, was held unconstitutionally vague in *General Motors Corp. v. Blevins*, 144 F. Supp. 381 (D. Colo. 1956).

the sole exception of the Colorado statute, wherein such words were held to be unconstitutionally vague,[12] these state statutes and the federal Act have withstood all constitutional challenges. Indeed, Chief Judge Aldrich, who wrote the opinion below, authored the leading opinion sustaining the validity of the federal Automobile Dealers' Day in Court Act. *Volkswagen Interamericana, S.A. v. Rohlsen*, 360 F.2d 437 (1st Cir. 1966).

Puerto Rico is the first jurisdiction to attempt to expand the scope of such legislation beyond automobile dealer franchises to encompass all types of dealer franchises; and it has done so using the federal statute as a model. At least three states, Massachusetts (H. 2279), New York (proposed Assembly Act No. 739) and California (S. 240), are considering similar legislation. In addition, a proposal (S. 1967, 91st Cong., 1st Sess.) is now pending in Congress to prohibit "bad faith" terminations by all types of franchisers. But the First Circuit's decision in this case has caused the Senate subcommittee considering S. 1967 "to indefinitely postpone" further action on the measure until this appeal is resolved (116 Cong. Rec. D501, May 19, 1970, Daily Ed.). The decision, moreover, has cast serious constitutional doubt on all the various state statutes and proposals dealing with franchise terminations. In fact, the decision, fairly read, seems to bring the federal Automobile Dealers' Day in Court Act under a constitutional due process cloud despite the earlier validation on other grounds in the *Volkswagen* case.[13]

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[12] See *General Motors Corp. v. Blevins*, 144 F. Supp. 381 (D. Colo. 1956). But in the instant case, the First Circuit stated that it did "not agree with the position of the opponents of the [Puerto Rican] act that the phrase 'just cause' is unconstitutionally vague and unspecific." See p. 39, *infra*.

[13] Chief Judge Aldrich sought in the opinion below to distinguish the federal Act from the Puerto Rican statute and thus to distinguish the *Volkswagen* ruling. See pp. 40-41, *infra*. He claimed that the federal Act does not convert terminable dealer contracts

(Footnote 13 continued on page 18.)

As will be seen, the constitutional grounds employed below to invalidate the Puerto Rican statute are at best tenuous and fully justify plenary review by this Court. But the importance and the impact of the decision below upon the federal and state legislative policies regarding dealer franchises are so great as to make such review most appropriate. And in Puerto Rico alone it has been reliably estimated that nearly 60 franchise terminations are or have been the subject of litigation in the federal and local courts; many of those cases that involve the constitutionality of the Dealer's Act have been stayed pending the outcome of the instant appeal.

The First Circuit itself recognized, pp. 32-33, *infra*, "the great importance of the [Puerto Rican] legislation," as a consequence of which "we issued a general invitation for amicus briefs" and "[m]any were filed." Its decision has served to enhance the importance of the problem and the need for review by this Court.

2. The decision below raises substantial issues of constitutional law and resolves them in a manner inconsistent with the decisions of this Court.

In essence, the First Circuit has held that the Puerto Rican Dealer's Act, by providing that existing franchises

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Footnote 13 continued:

into non-terminable ones but simply seeks to prevent contractually unjustified demands by giving a cause of action for damages resulting from unfair "coercion" and "intimidation." Actually, the same analysis could be made of the Puerto Rican statute.

But even so limiting the federal Act would not seem to meet the First Circuit's complaint in the instant case that established contractual rights cannot be altered retroactively. The contractual right to cancel the contract at will and without cause is no less altered by a statute outlawing such a right where the cancellation is motivated by "coercion" or "intimidation." The due process implications of altering that contractual right were not raised or explored in the *Volkswagen* case, however.

terminable at will can be terminated only for "just cause," constitutes a severe retroactive alteration of contractual obligations and hence violates the Due Process Clause of either the Fifth Amendment or the Fourteenth Amendment. That ruling constitutes a most questionable rearrangement of the United States Constitution and in the process resurrects constitutional doctrines long ago rejected by this Court. It would be unfortunate in the extreme if such a confused and unwarranted constitutional melange were left unreviewed and uncorrected.

A. The Constitutional Rearrangement

At the outset, the First Circuit is concededly unclear and uncertain whether Puerto Rico comes within the Due Process Clause of the Fifth Amendment or the Due Process Clause of the Fourteenth Amendment. This uncertainty is understandable in view of the rather unique commonwealth status of Puerto Rico and perhaps some definitive resolution of the problem by this Court is now appropriate. If that issue is deemed relevant by this Court, it would be appellant's position that, in view of the enactment of Public Law 600 in 1950 and the subsequent development of its commonwealth status, Puerto Rico may most appropriately be considered not as a federal enclave within the scope of the Fifth Amendment but as a state within the contemplation of the Fourteenth Amendment. See *United States v. Valentine*, 288 F. Supp. 957 (D.P.R. 1968); 98 Cong. Rec. 6183, et seq.

But the uncertainty exhibited in this respect by the First Circuit has constitutional repercussions that reach beyond Puerto Rico. The critical constitutional elision promulgated here is that "the due process clause of the federal constitution" provides "essentially the same restraint [as the Contract Clause, Art. I. Sec. 10] so far as retrospectivity is concerned." By thus importing at least part of the Contract Clause into "the due process

clause," the court has created a major constitutional adjustment of an uncertain nature:

(1) If the First Circuit in fact or by intention has transferred the retroactive aspects of the Contract Clause to the Due Process Clause of the Fifth Amendment, then a new and unwarranted limitation has been placed on the Federal Government, as well as on other federal jurisdictions that may be subject to that Amendment. This Court long ago recognized the power of Congress to regulate in the public interest the relationships between private parties under existing contracts that interfere with the exercise of its constitutional authority; the Fifth Amendment does not inhibit such impairment of contract. *Continental Illinois National Bank v. Chicago, R. I. & P. R. Co.*, 294 U.S. 648, 680 (1935).

(2) On the other hand, if the First Circuit meant to incorporate the retroactive aspects of the Contract Clause into the Due Process Clause of the Fourteenth Amendment, a needless but nonetheless confusing constitutional rearrangement has occurred. The states and other jurisdictions subject to the Fourteenth Amendment's Due Process Clause are already subject to the Contract Clause provision in Article I, Section 10, that "No State shall . . . pass any . . . Law impairing the Obligation of Contracts." The problems and the repurcussions of this novel transfer of one independent provision into another need not here be explored, but they are formidable.[14] Not the least of those problems is whether, as the First Circuit seemingly assumed, the Contract Clause is divisible into retroactive and non-retroactive parts so that a transfer thereof to the Due

[14]The First Circuit's statement that the Due Process Clause provides the same retrospective restraint as the Contract Clause was accompanied by no citation of authority. Suffice it to say that none exists. As respects the Fourteenth Amendment's Due Process Clause, however, the court may have confused Contract Clause doctrines with the freedom to contract—an entirely different concept that is incorporated in the Fourteenth Amendment. See *Alaska Packers Assn. v. Industrial Accident Comm.*, 294 U.S. 532 (1935).

Process Clause may be made only "so far as retrospectivity is concerned."

Such constitutional rearrangements, particularly of so confused a nature, certainly deserve consideration by this Court before they become embedded in federal jurisprudence.

B. The Contract Impairment and Due Process Misconceptions

The First Circuit has outlawed the Puerto Rican Dealer's Act by reliance upon what it conceived to be the constitutional concepts of due process and impairment of contract obligations. But the concepts were grossly misconceived and the relevant decisions of this Court were either misread or ignored.

The constitutional errors so patent in the opinion below stem principally from the court's refusal to give more than lip service to the established police power of Puerto Rico to safeguard what it conceives to be the vital interests of its people and its economy. The court acknowledged but rejected the public purposes underlying the legislation penalizing arbitrary cancellation of franchises—the frustration of dealers' legitimate expectations and interests, the resulting instability of local investments and export of profits, and the loss of some business to Puerto Rico's detriment.[15] See pp. 34-35, *infra*.

The First Circuit had earlier found that precisely the same type of considerations constituted "a sufficient public purpose" and "could be found to redound to the

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[15] The court also quoted from the Puerto Rico legislature's Statement of Motives, which stated that "reasonable stability in the dealer's relationship in Puerto Rico is vital to the general economy of the country, to the public interest and to the general welfare" and that it was necessary to regulate that relationship "so as to avoid the abuse caused by certain practices." See p. 34, *infra*.

ultimate benefit of the public at large" so as to justify the exercise of federal power in the form of the Automobile Dealers' Day in Court Act. *Volkswagen Interamericana, S.A. v. Rohlsen*, 360 F.2d 437, 445 (1st Cir. 1966). But in the Puerto Rican situation the court labeled such legislative considerations as mere "sounding phrases" and proceeded to make its own contrary determinations. The legislative assertion that arbitrary termination of dealership contracts frustrated the legitimate expectations of the dealers, said the court, "cannot possibly be true" since they "could have no legitimate expectation of non-terminable contracts." See p. 39, *infra*.

Having thus rejected the legislative findings, the court proceeded to treat the constitutional notions of contract impairment and due process in a manner that raises most serious problems worthy of this Court's review:

(1) The court viewed the contract impairment problem as one to be solved solely by a judicial determination of whether the alteration was "minor" or of "great magnitude." If the legislation "drastically" affected property or contract rights, said the court, there was in effect a *per se* violation of the Contract Clause.

Such an analysis of this constitutional proscription finds no precedent in the decisions of this Court. Rather, this Court has emphasized repeatedly that the prohibition "is not an absolute one and is not to be read with literal exactness like a mathematical formula," *Home Building & Loan Assn. v. Blaisdell*, 290 U.S. 398, 428 (1934), and is "qualified" by the state's "authority to safeguard the vital interests of its people," *Ibid.*, 434-435. And once the public interest in altering contracts has been asserted, as Puerto Rico has here done, a court "must respect the 'wide discretion on the part of

the legislature in determining what is and what is not necessary.'" *East New York Savings Bank v. Hahn*, 326 U.S. 230, 233 (1945). The critical factor thus is not the fact or the extent of the impairment but the reasonableness or necessity of the exercise of the state police power. See *El Paso v. Simmons*, 379 U.S. 497, 506-509 (1965).

(2) In transferring the constitutional prohibition against contract impairment into the contours of "the due process clause . . . so far as retrospectivity is concerned," the First Circuit has totally ignored the constitutional proposition that, in evaluating economic legislation in light of the Fourteenth Amendment's Due Process Clause, courts do not substitute their social and economic beliefs for the judgment of legislative bodies. That proposition, most forcefully restated in *Ferguson v. Skrupa*, 372 U.S. 726 (1963), completely undermines the First Circuit's rejection of the findings of the Puerto Rican legislature. As stated in *Day-Brite Lighting, Inc. v. Missouri*, 342 U.S. 421, 423 (1952), "the state legislatures have constitutional authority to experiment with new techniques; they are entitled to their own standards of the public welfare . . : so long as specific constitutional prohibitions are not violated and so long as conflicts with valid and controlling federal laws are avoided."

It thus becomes appropriate for this Court to remind the federal judiciary once again that neither the Contract Clause nor the Due Process Clause has the effect of overriding the power of the states, or of Puerto Rico, to establish regulations reasonably necessary to secure the general welfare of the community and the economy. By that established standard the Puerto Rican Dealer's Act cannot be considered violative of the Due Process Clause of either the Fifth or Fourteenth Amendment.

3. Serious problems stem from the failure to abstain from resolving the constitutionality of the Puerto Rican statute where (a) the Puerto Rico Supreme Court has not yet interpreted the statute, and (b) the factual record is too incomplete to permit precise formulation and application of constitutional rules.

The refusal of the courts below to abstain from resolving the constitutionality of the Dealer's Act pending an authoritative interpretation thereof by the Supreme Court of Puerto Rico constitutes a most serious matter warranting this Court's attention. It is a problem that is aggravated by the circumstance that the action of the Puerto Rican legislature has been invalidated in the context of an interlocutory appeal from the denial of a preliminary motion to dismiss, the facts relevant to the applicability of the statute not having been developed.

Without knowing which sections of the Dealer's Act might become pertinent once the facts of this case were developed, the First Circuit has engaged in a free-wheeling search for sections to interpret in a manner to lend support to its conclusion that the Act is invalid in its entirety.[16] That the court's interpretations are questionable and doubtful is not surprising, particularly in view of the absence of concrete facts by which to test the interpretations.[17] But the important point is that the

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[16] Section 6 of the Act, as originally adopted in 1964, provided that if any clause, paragraph, article, section or part of the Act be declared unconstitutional "said judgment shall not affect, impair or invalidate the rest of this act." But without sufficient facts to determine which sections of this Act were applicable, it is impossible to tell which sections, if any, are unimpaired by the decision below.

[17] Among the questionable interpretations of the Act advanced by the First Circuit are:

(1) The court gave a narrow and crippling interpretation of the critical statutory concept of "just cause" for franchise termination. See pp. 39-40, *infra*. But while its opinion is not authoritative, the Superior Court of Puerto Rico in the *Construction Machinery*

(Footnote 17 continued on page 25.)

First Circuit's interpretations are not and cannot be the authoritative interpretations. Only the Supreme Court of Puerto Rico can supply such interpretations. And only those authoritative interpretations, viewed in the context of a fully developed fact situation, should be subjected to the delicate process of constitutional adjudication.

While abstention is not an absolute requirement in any case of constitutional adjudication, its use in this case would appear especially appropriate by virtue of the following circumstances:

(1) Puerto Rico is a commonwealth and there exists "the unique historic relationship between the

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Footnote 17 continued:
case (see p. 57, *infra.*), has already indicated that this concept of just-cause is to be interpreted case by case and is dependent upon the particular facts of each case; the content of "just cause" is to be supplemented by precepts drawn from other laws of Puerto Rico and other doctrines of the civil law, such as impossibility of performance.

(2) The Act was said to provide that a Puerto Rico dealer's contract, "regardless of its provisions for termination was, with certain exceptions, renewable indefinitely at the option of the dealer, and imposed substantial damages upon a manufacturer who refused to accede." See p. 32, *infra.* But the Act does not in terms deal with options to renew indefinitely; nor is the Act concerned with simple failures to renew. All that the Act deals with is the injurious unfair practice of terminations without just cause.

(3) The Act was said to provide that a manufacturer "may never terminate, *regardless of the provisions of the contract,* or refuse to renew the dealership on an agreed expiration date, except for just cause." See p. 35, *infra.* But in fact the statute recognizes that the franchisor may legally terminate on the ground, among others, that the franchisee has failed to perform any of the essential obligations of the contract. See §278(d), definition of "just cause."

(4) The Act was said to be mandatory in its damages provision and to tie the hands of the court in assessing the amount of damages in a given case. See pp. 35-36, *infra.* But the damage section, §278b, itself states that indemnification is limited to the extent of damages caused the franchisee, and that the value of good will to be considered is to encompass any factor that will help establish "equitably" the amount of good will for which indemnification must be paid.

Congress and the Commonwealth of Puerto Rico" (*Katzenbach v. Morgan*, 384 U.S. 641, 658 (1966)). Respect for Puerto Rico's status and the necessity of avoiding any possible irritant in the relationship between the United States and Puerto Rico dictate that the federal judiciary refrain from acting hastily in voiding Puerto Rican legislation prior to an authoritative interpretation by the appropriate body, the Puerto Rico Supreme Court. See *Bonet v. Texas Co.*, 308 U.S. 462 (1940); *Bonet v. Yabucoa Sugar Co.*, 306 U.S. 505 (1939); *Alcoa Steamship Co. v. Perez Perez*, 295 F. Supp. 187, 197 (D.P.R. 1968). The avoidance of such possible irritants is a primary reason for invoking the abstention doctrine. See *Reetz v. Bozanich*, 397 U.S. 82, 86-87 (1970). As was said by Judge Maris, speaking for a three-judge district court in *Wackenhut Corporation v. Aponte*, 266 F. Supp. 401, 405 (D.P.R. 1967), affirmed, 386 U.S. 268:

> "We think that the application of the doctrine of abstention is particularly appropriate in a case such as the present one which involves the construction and validity of a statute of the Commonwealth of Puerto Rico. For a due regard for the status of that Commonwealth under its compact with the Congress of the United States, dictates, we believe, that it should have the primary opportunity through its courts to determine the intended scope of its own legislation and to pass upon the validity of that legislation under its own Constitution as well as under the Constitution of the United States."

(2) The special respect due Puerto Rico serves to underscore the classic reason why abstention is proper in these circumstances—the possibility that the Supreme Court of Puerto Rico might so interpret the statute as to

eliminate the federal constitutional objections discovered by the First Circuit.[18] Or the statute might be invalidated under the provisions of the Puerto Rican Constitution proscribing impairment of contracts or deprivations of property without due process of law (Article II, Section 7). Such issues under the Puerto Rican Constitution were encompassed by the motion to dismiss filed by the Ridge Tool Company. On that basis, abstention could be ordered while the parties repair to the Puerto Rican tribunals to secure an authoritative declaration as to the statute's meaning and its validity under the Puerto Rican Constitution. See *City of Meridian v. Southern Bell Tel. & Tel. Co.*, 358 U.S. 639, 640-641 (1959); *Reetz v. Bozanich*, 397 U.S. 82, 85-87 (1970).

(3) The desirability of awaiting an authoritative statutory analysis by the Puerto Rico Supreme Court is augmented by the retrospective gloss that the First Circuit gave to the statute. It is the first rule of construction "that legislation must be considered as addressed to the future, not to the past" and that "a retrospective operation will not be given to a statute" unless such be "the unequivocal and inflexible import of the terms, and the manifest intention of the legislature." *Union Pacific R. Co. v. Laramie Stock Yards Co.*, 231 U.S. 190, 199 (1913); *Greene v. United States*, 376 U.S. 149, 160 (1964). Thus a federal court should be most reluctant in the first instance to read a state statute as retrospective in nature. Before that analysis is used for constitutional adjudication, the authoritative local tribunal should be given the opportunity to affirm or deny the retrospective

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[18] For example, the "just cause" concept of the statute might be so broadly construed by the Puerto Rico Supreme Court that the statute, as applied to a particular case, could not be said to result in penalizing the original termination rights of the manufacturer.

thrust of the statutory language and the retrospective intentions of the local legislature.[19]

(4) Finally, the lower courts should have abstained from adjudicating the constitutional validity of the Dealer's Act in the absence of an established set of facts. Without such facts, a declaration as to the invalidity of an important Puerto Rican statute becomes an advisory opinion and a gratuitous frustration of the announced will of the Puerto Rican legislature.

No federal court should attempt a constitutional adjudication of a statute "unless absolutely necessary to a decision of the case." *Burton v. United States*, 196 U.S. 283, 295 (1905). But here the claims and the record could in no sense be said to have combined to create an inescapable federal constitutional controversy. The federal constitutional issues that were decided stemmed from a highly generalized claim in the motion to dismiss that the Dealer's Act was "void and unconstitutional," no reference being made to any clause of the Federal Constitution. See pp. 5-6, *supra*. And the resolution of the federal issues that did occur in the courts below took place in a factual vacuum. At no point in this proceeding has the record consisted of anything more than (a) the complaint, alleging generally that there was a franchise agreement between the parties that was terminated in 1966 illegally and without just cause, and (b) the motion to dismiss, containing general allegations of voidness and unconstitutionality.

There has never been any proof or concession of the sketchy facts set forth in the complaint. No answer has been filed and no defenses have been raised. There is

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[19] The Supreme Court of Puerto Rico should also have the opportunity to assess and evaluate the Dealer's Act as a segment in the Puerto Rican antitrust legislation. Possible antitrust implications of arbitrary franchise terminations might have an impact on the way in which the Dealer's Act is construed.

no claim or evidence regarding the contents of the alleged franchise agreement or the nature of its termination provisions. The record gives no certain clue to the circumstances of the creation and termination of the agreement. No one can say what defenses of a non-constitutional nature might be raised and become dispositive of the case. And no one can say precisely what provisions of the Dealer's Act will become operative once the facts are developed.

In short, there is no factual basis for refining or resolving the federal constitutional questions. Long ago this Court warned that federal courts should never "anticipate a question of constitutional law in advance of the necessity of deciding it" and should never "formulate a rule of constitutional law broader than is required by the precise facts to which it is to be applied." *Liverpool, New York & Philadelphia S.S. Co. v. Commissioners*, 113 U.S. 33, 39 (1885). And it gave that warning in circumstances identical to those here involved, where the "precise facts" had not yet been determined at an early stage of the litigation. See also *United States v. Raines*, 362 U.S. 17, 21 (1960).

The lower courts should thus have abstained from engaging in the important and delicate task of constitutional adjudication at least until the precise facts essential to that adjudication have been established. And the First Circuit's acceptance of the interlocutory appeal in these circumstances can only be viewed as an impermissible acceptance of an invitation "to enter into a speculative inquiry for the purpose of condemning statutory provisions the effect of which in concrete situations, not yet developed, cannot now be definitively perceived." *Electric Bond & Share Co. v. S. E. C.*, 303 U.S. 419, 433 (1938).

Corrective action by this Court is obviously necessary.

CONCLUSION

For these various reasons, the Court should note probable jurisdiction over this appeal. In the words of Rule 15(1)(f), "the questions presented are so substantial as to require plenary consideration with briefs on the merits and oral argument, for their resolution."

Respectfully submitted,

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United States Court of Appeals
For the First Circuit

No. 7422

ARTURO FORNARIS, JR.,

PLAINTIFF, APPELLEE,

v.

THE RIDGE TOOL CO. et al.,

DEFENDANTS, APPELLANTS,

and

THE COMMONWEALTH OF PUERTO RICO,

INTERVENOR.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF PUERTO RICO

Before ALDRICH, *Chief Judge*,
MCENTEE and COFFIN, *Circuit Judges*.

Edward M. Borges and *O'Neill & Borges* on brief for appellants.

Francisco de Jesus Schuck and *Fiddler, Gonzalez & Rodriguez* on brief for appellee.

Gilberto Gierbolini, Solicitor General, and *Ida Cardona-Hernandez de Orenstein*, Assistant Solicitor General, on brief for Commonwealth of Puerto Rico, intervenor.

Eduardo Negron Rodriguez and *Baragano, Trias, Saldana & Francis* on brief for appellant in No. 6876.

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Sutton Keany, Merrell E. Clark, Jr., Terrence H. Benbow, Robert W. Gray, McConnell, Valdes, Kelley & Sifre and *Winthrop, Stimson, Putnam & Roberts* on joint brief of appellee and Bristol-Myers Company et al., amici curiae in No. 6876.

Edward M. Borges, Philip A. Ryan, O'Neill & Borges and *Baker & McKenzie* on brief for Economics Laboratory, Inc., et al., amici curiae in No. 6876.

Thomas V. Koykka, Edward D. Crocker, Walter A. Bates, William W. Taft and *Arter, Hadden, Wykoff & Van Duzer* on brief for Eaton Yale & Towne, Inc., amicus curiae in No. 6876.

Stanley L. Feldstein, Salvador Antonetti Zequeira and *Nachman, Feldstein, Laffitte & Smith* on brief for La Electronica, Inc., et al., amici curiae in No. 6876.

Arturo Estrella and *Baragano, Trias, Saldana & Francis* on brief for Felix A. Rodriguez, Inc., amicus curiae in No. 6876.

Mariano Canales Delgado and *McConnie, Canales & Ferrer* on brief for Carlos M. Ruiz, amicus curiae in No. 6876.

March 17, 1970.

ALDRICH, *Chief Judge.* On June 24, 1964 the Puerto Rico legislature enacted the so-called Dealer's Contract Law known as Law 75. 1964 Laws of Puerto Rico, 4th Sess., at 231 (approved June 24, 1964). Its exact terms we will come to presently, but in effect this statute provided that a Puerto Rico dealer's contract with a "principal," hereinafter manufacturer, regardless of its provisions for termination was, with certain exceptions, renewable indefinitely at the option of the dealer, and imposed substantial damages upon a manufacturer who refused to accede. On June 23, 1966 the scope of the obligation was enlarged to forbid the manufacturer from performing, irrespective of the provisions of the contract, "any act detrimental to the established relationship." 10 L.P.R.A. § 278a (1968 supp.). In spite of this legislation a number of manufacturers acted to terminate or otherwise change their dealers' agreements, and much litigation has ensued. Because of diversity of citizenship the bulk, apparently, of the cases were removed to the district court, where the defendants raised constitutional and other defenses. The court resolved these defenses in the plaintiff's favor in *Ruiz* v. *Economics Laboratory, Inc.*, D.P.R., 1967, 274 F. Supp. 14, and in the defendant's favor, in a more limited situation, in *United Medical Equipment Corp.* v. *S. Blickman, Inc.*, D.P.R., 1966, 260 F.Supp. 912. In the *Blickman* case the plaintiff appealed, and because of the great importance of the legislation we issued a general invi-

tation for amicus briefs. Many were filed. We specially invited the Commonwealth to brief and argue the question of constitutionality, which it graciously did.

After argument, but before we had completed our opinion, the *Blickman* case (No. 6876) was settled, mooting the appeal. Thereafter we were asked to accept an interlocutory appeal in the present case pursuant to 28 U.S.C. § 1292(b). The parties did not request oral argument. By order we took the appeal on the briefs of the parties and transferred all earlier briefs, amicus and otherwise, filed in the *Blickman* case. We invited the Commonwealth to file a supplemental brief, which it has done. In addition, we have the benefit of the opinion of the Puerto Rico Superior Court in *Construction Mach. & Supplies Corp.* v. *Construction Mach. Co.*, decided December 23, 1968, upholding the act's constitutionality.

In the present complaint plaintiff Fornaris, a citizen of Puerto Rico, alleges that for twenty-nine years he had been the exclusive distributor in Puerto Rico of merchandise manufactured by the defendant The Ridge Tool Company, an Ohio corporation; that on November 26, 1965, effective as of April 15, 1966, defendant "cancelled and/or terminated, without just cause the distributorship contract," contrary to the law of Puerto Rico.[1] It is not alleged that the termination was contrary to the terms of the contract itself, and we assume that it was in accordance therewith, and that plaintiff's rights depend solely upon Law 75. Defendant moved to dismiss on the ground that this law is unconstitutional, stating various reasons therefor. The court denied the motion on the basis of its opinion in *Ruiz* v. *Economics Laboratory, Inc.*, *supra*, and defendant appeals.

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[1] This must have meant Law 75, as plaintiff's action was prior to the 1966 amendment. We do not, in this opinion, reach the amendment except to observe the obvious, that it presents many additional problems.

Before considering the precise terms of Law 75 it is pertinent to review the circumstances that led to its passage, and the declared purposes sought to be achieved. The legislature appended the following statement.

"STATEMENT OF MOTIVES

"The Commonwealth of Puerto Rico can not remain indifferent to the growing number of cases in which domestic and foreign enterprises, without just cause, eliminate their dealers, concessionaries [sic], or agents, as soon as these have created a favorable market and without taking into account their legitimate interests.

"The Legislative Assembly of Puerto Rico declares that the reasonable stability in the dealer's relationship in Puerto Rico is vital to the general economy of the country, to the public interest and to the general welfare, and in the exercise of its police power it deems it necessary to regulate, insofar as pertinent, the field of said relationship, so as to avoid the abuse caused by certain practices."

We take this statement to be a summary of, and to represent an adoption of, the unanimous Report of the Committee on Industry and Commerce recommending the act in the form that it was eventually passed. The committee stated that it proposed the law because terminating dealerships "as soon as these have created a favorable market for their products, frustrat[ed] the legitimate expectations and interests of those who have so efficiently fulfilled their responsibilities."[2] See, generally, 18 Diario de Sesiones, Asambla Legislativa (Camara), May 22, 1964, pp. 1723-25. With respect to the "reasonable stability in the dealer's relationship," further amplification is to be found in 34 Rev. Jur. de la U.P.R. 497, quoted at length in the *Con-*

[2] For this, and certain other quotations, we rely upon translations from the Spanish furnished by various parties and not contradicted.

struction Machinery opinion. Briefly, it was felt that cutting off dealers, with the manufacturer establishing its own sales office or branches, leads to instability of local investments and to the export of profits. Conversely, if manufacturers can terminate with impunity, some may withdraw altogether. Some Puerto Rico branches are marginal compared with other branches in the United States, and consequently are the first to be closed in case of declining business, to Puerto Rico's detriment.

We have gone into this background supplied by the parties not only because it shows the purposes of the act, illuminating the propriety, or possibly, impropriety, of its provisions, but also because of the assistance it may give in resolving doubts as to the statutory meaning. Law 75 itself is relatively brief. A manufacturer may never terminate, regardless of the provisions of the contract, or refuse to renew the dealership on an agreed expiration date, except for "just cause." Law 75, § 2, 1964 Laws of Puerto Rico at 232 (approved June 24, 1964).[3] "Just cause" is legislatively defined as substantial failure of performance by the dealer.[4] In case of breach of the statutorily imposed obligation, damages "shall be fixed on the basis"[5] of a specified list of items. Law 75, § 3. These are substantial, particularly with respect to awarding the dealer the entire good will value of the agency without inquiry or adjustment for what portion may have been due to the acts of

[3] "Notwithstanding the existence in a dealer's contract of a clause reserving to the parties the unilateral right to terminate the existing relationship, no principal or grantor may terminate said relationship or refuse to renew said contract on its normal expiration, except for just cause."

[4] "[J]ust cause: nonperformance of any of the essential obligations of the dealer's contract, on the part of the dealer, or any action or omission on his part that adversely and substantially affects the interests of the principal or grantor in promoting the marketing or distribution of the merchandise or service." Law 75, § 1(d).

[5] It was conceded during the oral argument of the *Blickman* case that the Spanish, "se fijará a base" is mandatory.

the manufacturer, or even of prior dealers. To this figure is added, cumulatively the Commonwealth concedes, the amount of profits for the past five years. Law 75, § 3(d).[6] There is no provision for mitigation should it appear that the dealer had successfully transferred into an equally profitable line. Even apart from such lack of offsets, the award of both good will and loss of profits amounts to duplication. The parties are precluded from agreeing otherwise. Law 75 § 4.

In upholding the constitutionality of the application of the act to the present defendant the district court, as did the superior court in the comparable case, relied upon the police power. There can be no question but that this power permits the legislature to remedy various economic evils. All courts recognize, however, that retrospective legislation, affecting established rights and relationships, presents an additional problem. While the legislature may prevent an employee willing to contract to work for a low wage from doing so, *West Coast Hotel Co.* v. *Parrish*, 1937, 300 U.S. 379, the retrospective imposition of a minimum wage would be quite a different matter. *See Luce & Co.* v. *Minimum Wage Board*, 1943, 62 P.R.R. 431, *aff'd* 1 Cir., 1946, 155 F.2d 983, where the court stated, in dictum, that a statute granting additional benefits for "services entered into and executed . . . before the same went into effect . . . would be unconstitutional, since it would deprive the employers of their property without due process of law." 62 P.R.R. at 449. We cannot agree with the many arguments,

[6] If the dealer has been in business less than five years, an appropriate multiple is provided to determine the equivalent of five years. It may be noted that the effect of this provision is exactly to contradict the declared reason for the act — that dealers are cut off "as soon as they have developed a favorable market." On that basis their past profits would be negligible. If, however, the dealer had not received this unfortunate treatment, but had been permitted a long, prosperous career to reward him for his entrepreneur services, then his award under this section would be substantial.

variously advanced, that the case at bar does not involve similar retrospectivity. If at the time that Law 75 was passed a manufacturer had contracts with dealers that he could terminate at will without liability, and thereafter, because in the opinion of the legislature such a result would deprive the dealers of their expectations based upon their having "so efficiently fulfilled their responsibilities" it must make substantial payments on termination, we can only regard this as increased payment for past services. Indeed, if it is not, it is an amendment of the contract to require an outright gratuity.

We need not deal with a constitutional prohibition against impairing the obligation of contracts,[7] because the due process clause of the federal constitution provides essentially the same restraint so far as retrospectivity is concerned.[8] We have no thought that Puerto Rico is in a more favored position in this respect than is a state or

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[7] The argument goes that Puerto Rico is not subject to certain constitutional restrictions because not a "state." *Cf. Buscaglia v. Ballester*, 1 Cir., 1947, 162 F.2d 805. However, the Puerto Rico Constitution contains a provision comparable in this respect to the federal Bill of Rights. Puerto Rico Constitution Art. II, § 7. Since this provision might be said to have been imposed by Congress, see Act Mar. 2, 1917, c. 145, § 2, 39 Stat. 951, as amended, 41 Stat. 1096, 47 Stat. 158, 48 Stat. 361, 61 Stat. 772, repealed, except for last paragraph, Act July 3, 1950, c. 446 § 5(1), 64 Stat. 320, an argument might be made in favor of the federal court's interpretative and enforcement powers by one route or another. By suggesting the question we do not suggest the answer.

[8] "Although there is no clause expressly forbidding the federal government to pass laws impairing the obligation of contracts, any federal law impairing them in a manner which the Supreme Court deemed unreasonable would doubtless be held to be a deprivation of property without due process, contrary to the Fifth Amendment." Hale, The Supreme Court and the Contract Clause: III, 57 Harv. L. Rev. 852, 890 (1944). *Accord*, Hochman, The Supreme Court and the Constitutionality of Retroactive Legislation, 73 Harv. L. Rev. 692, 695 (1960); *Cf. Lynch v. United States*, 1934, 292 U.S. 571, 579; *Thorpe v. Housing Authority*, 1969, 393 U.S. 268, 278-79, nn. 31-32.

the federal government. *Figueroa Ruiz* v. *Delgado*, 1 Cir., 1966, 359 F.2d 718, 723-24, *Mora* v. *Mejias*, 1 Cir., 1953, 206 F.2d 377, 382. *See* 48 U.S.C. § 731d; Joint Resolution, 66 Stat. 327. (July 3, 1952). Hence only minor infringement of established contractual rights may be effected without just compensation. "Police power" is not a magic word that permits the legislature to adjust any and every found economic ill without payment.

In determining whether retroactive alteration of contractual provisions are sufficiently minor to be permissible a distinction is sometimes drawn between alteration of substantive rights and alteration of procedures or remedies. *See Stockholders of Peoples Banking Co.* v. *Sterling*, 1937, 300 U.S. 175, 180-83 (alternative holding). However, even the latter may infringe constitutional rights, Hale, *supra* n. 8, at 533-57, *W. B. Worthen Co.* v. *Kavanaugh*, 1935, 295 U.S. 56, while the former can sometimes be tolerated if the effect is not too severe. *El Paso* v. *Simmons*, 1965, 379 U.S. 497, 503-09. Essentially, the question is, how drastically have property rights been affected, and, particularly, how great is the change viewed in the light of the reasonable expectations of the parties when the contract was entered into. *See El Paso* v. *Simmons*, *supra*; *Home Bldg. & Loan Ass'n* v. *Blaisdell*, 1934, 290 U.S. 398. The distinction is one of degree. For example, emergency statutes allowing a tenant to stay beyond the term of his lease upon payment of reasonable rent have been upheld as reasonable alterations, *Block* v. *Hirsh*, 1921, 256 U.S. 135; *Marcus Brown Holding Co.* v. *Feldman*, 1921, 256 U.S. 170, whereas a statute which would have destroyed a mining company's reserved right to mine coal underneath land, the balance of which had been sold by it, has been invalidated as working a change of too great magnitude. *Pennsylvania Coal Co.* v. *Mahon*, 1922, 260 U.S. 393. See generally Hochman, *supra* n. 8, at 711-17.

While we recognize a strong obligation to support legislative findings, the Report of the Committee on Industry and Commerce to the effect that the termination of dealerships in terms revocable at will was "frustrating the legitimate expectations" of the dealers cannot possibly be true. Dealers may have had hopes; they could have no legitimate expectation of non-terminable contracts. *Cf. Castillo v. Smart Products, Inc.*, D.P.R., 1968, 289 F.Supp. 138. Sounding phrases, and calling the failure to make termination payments an "abuse," cannot change the fact that the manufacturer has been forced into heavy contractual obligations that it never assumed. No amount of research by parties or amici has discovered a case suggesting that to convert a contractual relationship terminable by either party without cause into one which, short of breach by the other party, can be terminated by one of the parties only by making substantial payments and without protection for the other party's economic interests, is not a change of great magnitude.[9]

We do not agree with the position of the opponents of the act that the phrase "just cause" is unconstitutionally vague and unspecific. However, the Commonwealth's protestation, in the *Blickman* brief, that it "cannot conceive that the Legislature, which was enacting a remedial statute to correct an injustice, could have intended and permitted, through legislation, the perpetration of another injustice," is far more pious than persuasive. To our comment that the statute is one-sided, the Secretary of Justice on behalf of the Commonwealth, urged us to read it in the light of various general provisions of Puerto Rico law applicable

[9] If we may be forgiven a rude comparison, the change seems comparable to a legislative retrospective conversion, in the asserted interest of public morals, of all temporary liasons into marriage, with the necessity of divorce and alimony. Indeed, it is worse, for until Law 75 was enacted temporary dealerships were in all respects legal.

to the construction of contracts. This we have done. We end up convinced that the only defense open to a manufacturer to an action under Law 75, short of proof of breach by the dealer, would be impossibility of performance. 31 L.P.R.A. § 3193. To add to "just cause," as was suggested, good faith, or the legitimate interests of the manufacturer, would be to fly in the face both of the unambiguous statutory provisions, and the equally unambiguous legislative history. The fact that a dealership has become economically highly disadvantageous is not excusable impossibility, but is, precisely, a contingency that the legislature sought to guard against.

Some of the proponents of the act invite a comparison with the federal Automobile Dealers Day in Court Act, 15 U.S.C. § 1221-25, hereinafter the Federal Act. The comparison is ill-taken. In fact, it is precisely to the extent that Law 75 departs from the provisions of that statute that it is in difficulties.

The unusual position in which automobile dealers find themselves has long been known to this court.[10] Because they are normally locked in, with no other source of income and no easy opportunity to convert to other lines, an unscrupulous manufacturer is able to take advantage of its dealers by making unjustifiable demands, such as requiring needlessly large showrooms, or the purchase of undesired parts or models, under threat of cancellation of the dealership. It was found that many manufacturers were engaging in such practices. See generally, Kessler, Automobile Dealer Franchises: Vertical Integration by Contract, 66 Yale L.J. 1135 (1957). The Federal Act did not seek to convert terminable automobile dealers contracts into nonterminable ones, but was tailored to prevent contractually

[10] *See Volkswagen Interamericana, S.A.* v. *Rohlsen*, 1 Cir., 1966, 360 F.2d 437, *cert. denied* 385 U.S. 919; *Young Motor Co.* v. *Com'r*, 1 Cir., 1960, 281 F.2d 488.

unjustified demands by giving a cause of action for damages resulting from unfair "coercion" and "intimidation." 15 U.S.C. § 1221(e). Absent such improper behavior, any action within the terms of the contract remained permissible, including outright termination without proof of grounds therefor. *Berry Bros. Buick, Inc.* v. *General Motors Corp.*, E.D.Pa., 1966, 257 F.Supp. 542, 546, *aff'd mem.* 3 Cir., 1967, 377 F.2d 552; *cf. Southern Rambler Sales Inc.* v. *American Motors Corp.*, 5 Cir., 1967, 375 F.2d 932, *cert. denied* 389 U.S. 832; 15 U.S.C. §§ 1221, 1222.

By contrast, Law 75 applies to every kind of dealer across the board. As pointed out in the memorandum opinion of the district court in *Felix A. Rodriguez, Inc.* v. *Bristol-Myers Co.*, D.P.R. 2/13/68, many types of dealers carry numerous articles and lines, or can readily convert and absorb the loss of a single manufacturer. Such dealers are not subject to pressure by threats of cancellation. Nor was the Puerto Rico act framed in terms of illegitimate demands—except to say that adherence to the contract terms was itself illegitimate. By labelling the exercise of express contractual rights "unjust" the legislature was not giving a cause of action for contractual abuse; it was re-writing the contract.

Comparing Law 75 with the Federal Act in terms of retrospectivity is, in a sense, merely an intellectual exercise. The parties have cited no case holding even the Federal Act constitutionally retrospective. Non constat, in the light of the differences, that it might properly be so held had the question arisen.[11] Law 75, however, cannot be.

The judgment of the District Court is vacated. Judgment for the defendant.

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[11] We do not reach the question of non-retrospective application of Law 75, as we may wonder how many such dealerships have been established. Since the provisions of the law are non-waivable, manufacturers who are unwilling to accept them will not enter into dealer-

ship contracts at all, and dealers who would prefer to have dealerships omitting such benefits rather than have none, have lost, to that extent, their freedom of contract. It is possible that if the legislature had realized that the law could be applied only prospectively it would not have enacted it. With this matter, however, we are not presently concerned.

Adm. Office, U. S. Courts — Blanchard Press, Inc., Boston, Mass.

On the same day, March 17, 1970, the following judgment was entered:

JUDGMENT

Entered March 17, 1970

This cause came on to be heard on appeal from the United States District Court for the District of Puerto Rico and was submitted to the Court.

Upon consideration whereof, It is now here ordered, adjudged and decreed as follows: The judgment of the District Court is vacated and the case is remanded to that Court with directions to enter judgment for the defendants.

By the Court:

/s/ Dana H. Gallup

Clerk.

Enter:

/s/ Aldrich, Ch.J.

UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

ARTURO FORNARIS, JR.	)	
	)	
Plaintiff, Appellee	)	
	)	
v.	)	
	)	
THE RIDGE TOOL COMPANY, et al	)	
	)	CIVIL NO. 7422
Defendants, Appellants.	)	
	)	
and	)	
	)	
THE COMMONWEALTH OF PUERTO RICO	)	
	)	
Intervenor, Appellee.	)	

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

To the Honorable Court:

1. Notice is hereby given that Arturo Fornaris, Jr., Plaintiff, Appellee above named, hereby appeals to the Supreme Court of the United States from the judgment opinion entered by this Honorable Court on March 17, 1970.

2. This appeal is taken pursuant to 28 U.S.C. §1254(2). In San Juan, Puerto Rico, this 29th day of April, 1970.

Francisco de Jesus Schuck

[Proof of Service omitted]

Filed in United States
Court of Appeals
for the First Circuit

May 4, 1970

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF PUERTO RICO

ARTURO FORNARIS, JR.,	)	
	)	
Plaintiff	)	
	)	
vs.	)	
	)	
THE RIDGE TOOL COMPANY AND THE RIDGE TOOL INTERNATIONAL COMPANY, INC.	)	CIVIL NO. 546-66
	)	DAMAGES
	)	
Defendants	)	
	)	
THE COMMONWEALTH OF PUERTO RICO	)	
	)	
Intervenor	)	

MEMORANDUM AND ORDER

On March 12, 1968 this Court entered an order staying proceedings in this action pending determination of an action entitled *United Medical Equipment Corporation vs. S. Blickman, Inc.*, which at that time was pending before the Court of Appeals for the First Circuit, Case Number 6876, and wherein the constitutionality of Law Number 75 of June 24, 1964, as amended (10 L.P.R.A. 278), was being challenged on the same grounds as those raised by the defendants in this case through their motion to dismiss. The matter of the constitutionality of the Dealer's Act was fully briefed and all argument was had before the Court of Appeals, but the case was settled prior to decision.

A similar fate befell the case of *Carmac Chemical Corporation v. Application Engineering Corporation* (Court of Appeals for the First Circuit, Case Number 7177). In this case, the First Circuit, as per Order of Court, August 29, 1968, took the position that it would appreciate an opportunity to consider the views of at least the Superior Court of Puerto Rico on the constitutionality of the Dealer's Act. Accordingly, it neither allowed nor denied the interlocutory appeal and stated that upon receipt of any decision and opinion from the Superior Court of Puerto Rico, and upon a joint stipulation or a deposition or other showing of the terms, conditions and surrounding circumstances, the Court would again consider the application for leave to appeal in the *Carmac* case. Once again the parties settled the case and there is now no case pending before the United States Court of Appeals which raises the constitutionality of the Dealer's Act.

The matter of the constitutionality of the Dealer's Act has now been passed upon by the Superior Court of the Commonwealth of Puerto Rico in the case of *Construction Machinery and Supplies Corporation v. Construction Machinery Co.*, Civil Number 67-3549. A translation of this case is set out as Exhibit A to this order, and made to form a part hereof by reference.

A motion for reconsideration of the Superior Court Order was denied on March 11, 1969 by said Tribunal.

In view of the foregoing developments, this Court ordered that this case be set for some disposition and set a hearing thereon for June 13, 1969. By motion dated June 9, 1969, attorneys for the plaintiff requested that on the basis of the decision rendered by the Superior Court of Puerto Rico in the case of *Construction Machinery and Supplies Corp. v. Construction Machinery Co.*, *supra*, and on the basis of this Court's prior decision upholding the constitutionality of the Dealer's Act of Puerto Rico we order the dismissal of defendant's

motion to dismiss and order the defendants to file their answer to the complaint filed in this case.

We agree with plaintiff that the motion to dismiss should be denied on the basis of our prior decision in this area [*Ruiz v. Economics Laboratory, Inc.*, 274 F. supp. 14 (1967)]. This Court is of the opinion that the order of dismissal of the constitutional defense raised by the defendants involves a controlling question of law as to which there is substantial ground for difference of opinion in this jurisdiction and that an immediate appeal from this order may materially advance the ultimate termination of this litigation and of many others presently pending in this Tribunal. In conformity with 28 U.S.C.A. §1292(b) and inasmuch as a rapid adjudication of the constitutionality of the Dealer's Act is not only in the best interests of the parties to this action, but is also in the furtherance of justice, it is hereby

ORDERED

1. Defendant's motion to dismiss on constitutional grounds is denied (*Ruiz v. Economics Laboratory, Inc.*, 274 F. Supp. 14 (1967) *Construction Machinery and Supplies Corp. v. Construction Machinery Co.*, Civil Number 67-3349, Superior Court of Puerto Rico, San Juan Part).

2. This Court is of the opinion that this order involves a controlling question of law as to which there is substantial grounds for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation. Accordingly, this Court hereby so states as required by Section 1292(b) of Title 28 U.S.C.A.

3. All further proceedings in this case are stayed until further order of this Court.

San Juan, Puerto Rico, this 8th day of August 1969

/s/ Hiram R. Cancio
HIRAM R. CANCIO
CHIEF JUDGE
UNITED STATES DISTRICT COURT

IN THE SUPERIOR COURT OF PUERTO RICO
SAN JUAN PART

CONSTRUCTION MACHINERY & SUPPLIES CORPORATION

Plaintiff,

vs.

CONSTRUCTION MACHINERY CO.

Defendant

Re: DAMAGES

COMMONWEALTH OF PUERTO RICO

Intervenor

OPINION

The matter before the court is a special defense filed by defendant in this case on May 13, 1968 in which there is alleged the unconstitutionality of Law § 75 of 1964, as amended.[1]

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[1] The circumstances that led to the intervention by the Legislature of Puerto Rico are amply set forth in 34 Rev. Jur. de la U.P.R. p. 497. The following appears there:

> "Law No. 75 of June 24, 1964 is of great importance for contractual relationships between principals and distributors in Puerto Rico. We shall study two aspects of it. First, the manner in which said contracts are affected by the law. Second, the constitutional issues raised by the same. This second part of the study will be carried out by means of a comparative analysis of other similar laws that are in effect in different jurisdictions of the United States.

(Footnote 1 continued on page 50.)

After having studied the memoranda of the parties, as well as the oral argument, we may pass on to consider the allegations.

Footnote 1 continued:

Similarly, the jurisprudence which has arisen in connection with these statutes will form a part of our analysis.

The social ill that this piece of legislation seeks to correct is based upon the fact that a great number of distributors based in Puerto Rico have been eliminated as factory representatives. This tendency caused the voices of the Chamber of Commerce of Puerto Rico and of the individual distributors to be heard in protest against the existing situation. Said tendency is characterized by two types of situations: principals or grantors that arbitrarily cancel the distribution contracts of businessmen established in Puerto Rico; and the factories that decide to open their own sales offices or branches. The distributors faced these problems espousing several arguments. This group maintains that the development of a market for the represented products requires great sums of money. That once the products are on the market, the factories, not withstanding the effort and the capital invested, cancel the contracts and establish themselves here without providing any indemnity whatever. It is pointed out that the system by means of which the manufacturers establish sales offices or branches creates an instability that impedes the strengthening of the field of local capital investment. It is also said that when branches or sales offices are established, these export a large part of the profits earned in Puerto Rico.

Some of the established branches are classified as marginal branches. These are the sales offices located in markets that are small when compared to other branches in the United States. They are the first to be closed in time of emergency, which would force Puerto Rico to recur directly to the northamerican market to obtain indispensable items, especially in the field of industry. This class also incurs greater general expenses relative to sales and the product which would result in a price increase and a reduction in services.

Local distribution serves as an incentive to those persons who won't have their own business. A manager of a branch cannot become interested in the problems, ambitions and needs of our community. The distributors claim that the manager of a branch has as his

(Footnote 1 continued on page 51.)

1. The defendant alleges that Act No. 75 of 1964 impairs the obligations of contracts existing at the time of its approval.

Footnote 1 continued:

purpose the securing of a promotion to be sent to another country or to the home office as an executive and, for that reason, is not interested in the well-being of the Puerto Rico economy. The persons in charge of the sales office do not fully know the motivations or factors that motivate the decisions that must be put into effect, inasmuch as these are made by the Board of Directors at the home company. Said decisions may very well result in a detriment to the Puerto Rico market due to the fact that standards and methods used in the northamerican nation are not necessarily applicable to our market. The distributor established in Puerto Rico by his very nature and experience is more familiar with the country's market. We can say that he knows the psychology of the consumer. As a result this singular position allows the person to adequately determine the preferences of the consumer in terms of the type of product desired and the amounts that may be consumed, thus maintaining a beneficial balance for the economic stability of our community.

Those who are opposed to a system of distribution of products and services through exclusive distributors claim that it is an unnecessary and expensive middle step that only contributes to an increase in the costs of distribution. The opposing side argues that it is an indispensable factor for the marketing system. This is based upon the following: Due to our insular condition to the fact that our market is separated from the principle sources of supply by an enormous stretch of sea, to our geographical smallness and lack of natural resources and because potential sales and business volume in our island is relatively small, to the manufacturer it would normally be uneconomic to eliminate the exclusive agent or distributor and establish its own branch for sales, or to sell to consumers from its point of origin or to local wholesalers and retailers. The exclusive agent or distributor is a functional intermediary that with the exception of certain isolated cases, may not be eliminated or cut back without causing injury to the efficiency and costs of our distribution system, for they render important services in an atmosphere of competition to the producer and the consumer in a manner more efficient and economic than the very manufacturers."

(Footnote 1 continued on page 52.)

In support of this allegation the defendant cites the provisions of Article 1207 of the Civil Code and the first article, tenth section of the Constitution of the United States of America and the second article, seventh section of the Constitution of the Commonwealth of Puerto Rico.

The provisions cited above have not been violated by this Law of the Legislature of Puerto Rico. It is a principle recognized by the courts of Puerto Rico and of the United States of America that this right of freedom of contract is not one without limit of any kind. The

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Footnote 1 continued:

The circumstances set forth above led the legislature to act. It was forced to resolve the problem put to it by a pressure group: the need to stop the principals, or at least to seek indemnification for the distributors. It was the practice to include a clause, in which it was provided that either of the parties by means of 30, 60, or 90 days notice could cancel the existing relationship. The principal, making use of its bargaining power, managed to include in the contract this and other clauses favorable to it.

In order to remedy this situation, the Legislative Assembly of Puerto Rico, invoking the police power of the State, approved the law now before us for the purpose of regulating the termination of distribution contracts and a refusal to renew the same. The statute expressly provides that no principal or grantor may unilaterally terminate a distribution contract or refuse to renew the same without just cause, notwithstanding any agreement to the contrary.

If the principal or grantor terminates the contractual relationship, without just cause, it must indemnify the distributor. The rights granted by the law are of a public nature, and therefore not waivable. All actions based upon the law prescribe in three years reckoned from the date of the definitive termination."

In light of the foregoing examination it is evident that the problems and needs of Puerto Rico are in large measure different from those of the United States of America and the existing relationship between the two requires a more equitable and special consideration in order to arrive at the conclusions of this opinion. We can not forget that Puerto Rico is a small island (3,500 square miles), tropical, with few natural resources, depending, for this reason, greatly upon business".

same is conditioned by the police power of the state. Article 1207 of our Civil Code contemplates this when it provides that:

> "The contracting parties may make the agreements and establish the clauses and conditions which they may deem advisable, provided they are not in contravention of law, morals of public order". (31 LPRA 3372)

In *Manigault v. Spring*, 199 U.S. 473 (1905) it was noted that:

> "This power . . . is an exercise of the sovereign right of the government to protect the lives, health, morals, comfort, and general welfare of the people, and is paramount to any rights under contracts between individuals".

Reference may also be made to *Sierra v. San Miguel*, 1949, 70 P.R.R. 573, in which the Honorable Supreme Court of Puerto Rico referring to the same question notes that "no rule is more firmly embedded in our constitutional law than this doctrine". See further, *Veil v. Sixth Ward Building*, 310 U.S. 32; *Anderson v. Brand*, 303 U.S. 95; *City of El Paso v. Simmons*, 379 U.S. 497.

Law No. 75 was created to remedy an existing "grave situation" that would still exist if it were not for the promulgation of said law. See page 1531 of the Record of Meetings of the Legislative Assembly of Puerto Rico of 1964 where it is said:

> "Your Committee on Industry and Commerce has considered the substitute to S.B. 673 and has the honor of proposing that it be approved without amendment.
>
> The problem created in the system of distribution in Puerto Rico by the intemperate action of foreign and domestic business concerns that, without just cause, cancel their

relationships with their distributors and agents in Puerto Rico, as soon as those have created a favorable market for their products, frustrating the legitimate expectations and interests of those who have so efficiently met their responsibilities, has recently worsened.

Normally, the agency or distribution contract is drafted by the manufacturer with clauses favorable to it, and a provision to the effect that the relationship may be terminated by either of the parties, by means of prior notice of sixty or ninety days. The distributor or agent efficiently devotes himself to opening the market for the represented product, and, when he begins to derive benefits from the operation, once the market is established, the manufacturer realizes that it would be economically favorable to establish its own sales office or its own branch, and in an unjust manner, without equitable compensation for the efforts expended by the distributor or agent, cancels the relationship. In other cases, the manufacturer finds another person who, the business being established, is willing to distribute the product for less compensation, because he doesn't have to make the initial investment, and is not subject to the risks of the prior distributor or agent.

The traditional provisions which regulate contracts between private parties have shown themselves to be incapable of protecting the legitimate rights of the distributor or agent, and for this reason it has become necessary to legislate to regulate this relationship and guarantee that the manufacturers will act in good faith, equitably, in a non-arbitrary manner, and to preserve for the distributor or agent the legitimate rights and expectations

inherent in the relationship. Moreover, this will result in greater stability for the distribution relationship.

This is the grave situation that is sought to be remedied by the approval of this bill. The Department of Commerce of the Commonwealth of Puerto Rico, the Chamber of Commerce of San Juan, and the Agency for Industrial Development regard with accord and heartily endorse the protection and stability that would be given to the relationships between manufacturers and their distributors if this bill should be approved.

The Committee, unanimously, agreed to recommend the passage of this bill".

The defendant has noted that in said legislation the word "emergency" has not been used to justify the existence of said legislation. The expression "grave situation" within our language and culture and the interpretation which this Court makes of the legislative intent has a meaning similar to the English term "emergency"; assuming, but without deciding, that the appearance of this term is an indispensable requirement. The Spanish term "emergencia" as a translation of the English term "emergency" is an anglicism.[2]

In the case of *Willy's Motor v. Northwestern Kaiser–Willy's, Inc., 142 F. Supp. 469 (D.C.–1956)* there was contested the constitutionality of a Minnesota statute which contained greater requirements as to the relationship between manufacturers and distributors and at the same time covered a more restricted area than that covered by Law No. 75. The Court, in sustaining the constitutionality of the Minnesota statute, noted that

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[2]The Dictionary of the Royal Academy, eighteenth edition, defines the term "emergencia" as the act or result of emerging, occurrence, a supervening accident.

legislation enacted with a public purpose was not subject to attack under the Contracts Clause.

Law No. 75 has a public purpose, as can be clearly seen from its legislative history as well as from its statement of motives,[3] for this reason, we are of the opinion that the law does not suffer from the constitutional vice alleged and discussed above.

II. The defendant alleges as the second ground for the unconstitutionality of Law No. 75 that the Law violates the Due Process Clause as to manufacturers and that it is vague and imprecise as to its scope and definition of the term "just cause".

The standard to be used must be the reasonableness of the legislation. If the measure which we are considering is justified by social, economic, health, or general welfare considerations, and it is reasonable the statute must be considered to be invulnerable to attacks of this sort.

In the case of *Blenke Brothers v. Ford Motor Co.*, 203 F. Supp. 670 (1962) the Court concluded that "the fact that Congress. . gave the dealer a remedy. . without giving the same remedy to the manufacturer, is not violative of the due process clause. . .". See to the same effect the case of *Kuhl Motors Co. v. Ford Motor Co.* 71 N.W. 2d 420.

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3 "Statement of Motives"

The Commonwealth of Puerto Rico can not remain indifferent to the growing number of cases in which domestic and foreign enterprises, without just cause, eliminate their dealers, concessionaries, or agents, as soon as these have created a favorable market and without taking into account their legitimate interests.

The Legislative Assembly of Puerto Rico declares that the reasonable stability in the dealer's relationship in Puerto Rico is vital to the general economy of the country, to the public interest and to the general welfare, and in the exercise of its police power, it deems it necessary to regulate, in as far as pertinent, the field of said relationship, so as to avoid the abuse caused by certain practices".

The defendant alleges that Law No. 75 in its definition of just cause is unreasonable, arbitrary and capricious, vague and imprecise. Said definition is not limited to its literal content. It constitutes a guide to the Court so that it may decide in the light of the facts of each particular case whether or not there existed just cause. This concept of just cause just like the concept of the reasonable man and the good head of a family is not a new concept in our law.

In the cases of *P.R. Cap. S. Tire Sales v. District Court*, 1948, 68 P.R.R. 370; *Aviles v. District Court*, 1948, 69 P.R.R. 106; *Blanes v. District Court*, 1948, 69 P.R.R. 106; *Mercedes Bus Line, Inc. v. District Court*, 1949, 70 P.R.R. 656, our Supreme Court considered the concept of "just cause" in accordance with the facts of each case brought before its consideration. In each of these cases it can be appreciated how wide this concept of just cause is; as well as its usefulness in our system. The use of this concept in various laws is due to the fact that the legislature cannot foresee every possible fact situation when it drafts a law, leaving this function to the courts who must decide in accordance with the particular facts of each case. This Court cannot understand that the legislator has imposed as the only reason justifying a cancellation of the relationships the reasons which make up the definition of just cause.

This concept of just cause, in its turn, should further be supplemented, when a case may merit it, with statutory precepts drawn from other laws of the State. Such would be the case of a manufacturer who for economic reasons cannot continue to sell its products in our market. In a situation like this one, this Court is of the opinion that it would be necessary to go beyond the law and make applicable the provisions that are relative to the impossibility of performance contemplated by our Civil Code, in Art. 1138 (31 LPRA 3193). See *Rodriguez v. Municipality*, 75 P.R.R. 449, where the Supreme Court of Puerto Rico says that:

"The impossible performance is produced when, having examined the circumstances on which a contract is signed and the circumstances on which it should be subsequently performed, it appears that its subsequent performance is not possible because of the supervening circumstances which did not exist at the time of contracting the obligation".

Summarizing, this concept of just cause must be interpreted case by case and always depending upon the particular facts of each one.[4] Obviously our own juridical system provides for cases in which compliance becomes impossible, and for this reason it is not correct to suppose that Law No. 75 of 1964 is unjust or oppressive in its terms.

There is nothing in the law that might be interpreted as indicating that the Legislature of Puerto Rico is discriminating against firms operating in interstate commerce. The law applies both to local firms and continental ones doing business in Puerto Rico. The present legislation is clearly within the police power which the Commonwealth of Puerto Rico possesses and within the clear intention of the Legislature of Puerto Rico to protect its citizens and businessmen.

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[4] Recently the Federal District Court for Puerto Rico, by the Hon. Judge Fernández Badillo expressed the same thought in the case of Schering Transamerican Corporation vs. Wallace Torres Canet vs. Sutton Cosmetics, et. al., Civil No. 542-66 in noting in its opinion of September 30, 1968 the following:

"Defendant does not claim that Sutton Cosmetics could not have whatever arrangement it had with him. Certainly when Sutton Cosmetics went out of business, that was ample 'just cause' to terminate whatever relationship they had".

"Nor does it preclude a state from giving needful protection to its citizens in the Course of their contacts with business conducted by outsiders when the legislation by which this is accomplished is general in its scope, is not aimed at interstate or foreign commerce, and involves merely burdens incident to effective administration".

It is worthy of note that in our commercial relations with the United States, Puerto Rico has received special treatment from the United States. Examples of this, among others, are the tariff laws dealing with sugar, coffee and rum exported from Puerto Rico. These and other similar laws, are founded upon the geographic and economic conditions of Puerto Rico and the lack of adequate natural resources, all of which has justified the special treatment as regards the other states of the Union.

IV. Defendant alleges that Law No. 75 violates the equal protection clause. The defendant further argues in its brief that the law in question operates for the sole and exclusive benefit of those distributors in existence at the time of its approval and that the manufacturers may not appoint additional distributors.

The equal protection clause does not imply that at any given moment the Legislature of a country may not establish a counterbalance in favor of a disadvantaged class.

In the case of *Kuhl Motor Co. v. Ford Motor Co. (supra)*, the following was noted:

> "The fact that the persons to be benefited by this regulatory measure are confined to one class of our citizens, auto dealers, does not militate against the same being a legitimate exercise of the police power".

There exists in Puerto Rico and the United States a great quantity of legislation which is directed to the benefit a particular class of individuals or persons. To contend that this may not be done is to bind the arms of the State in its mission to make all citizens equal in law.

There is nothing in this law that would lead this Court to think that new distributors may not be appointed inasmuch as the statute does not prohibit such action.

What the law regulates is the termination of the existing relationship: or directly or indirectly executing an act which impairs the established relationship: or a refusal to renew said contract upon its normal expiration. (10 L.P.R.A. 278a).

The case before us does not involve the appointment of an additional distributor. It deals with the termination of a distribution contract. At the proper moment we will decide whether there existed or not just cause. There may be circumstances in which the appointment of a new distributor constitutes an impairment of the established relationship, but courts should not deal with hypothetical situations. This Court is of the opinion that if the manufacturer or principal names a new distributor and there is no impairment of the existing relationships between it and the original distributor, said distributor is totally lacking a cause of action under this law. *We have already said that Law No. 75 is one which should be interpreted case by case and that only after the presentation of the whole evidence will the Court be in a position to determine whether there was an impairment of the existing relationship, or if there was a unjustified refusal to renew a contract or if a contract was terminated without just cause.*

The defendant alleges that Law No. 75 creates a monopoly in favor of the distributor. We do not see the logic of this observation. When an act, or series of acts in a particular case result in a monopoly or monopolistic practices prohibited by law, we will decide that problem in the light of the particular case. Neither the legislative history of Law No. 75, nor Law No. 77 of June 25, 1964, known as the monopoly law, provide a basis for this assertion. These laws were enacted contemporaneously so the legislators were aware of the contents and language of each when they were approved.

In connection with the damages contemplated by Section 278 b of the law (Title 10 L.P.R.A.), we are of the opinion that the same does not limit the power of

the Court to indemnify a distributor upon the basis of the factors set forth in the said section.

For the reasons set forth, the Court concludes that Law No. 75 of 1964, as subsequently amended meets the constitutional requirements. The special defense pleaded by the defendant is therefore denied.

Let service be made.

Given at San Juan, Puerto Rico, this 23rd of December, 1968.

(s) Hector Ruiz Somohano
Superior Court Judge

PUERTO RICAN DEALERS' CONTRACT ACT

10 L. P. R. A. § 278, et seq.

§ 278. Definitions

For the purposes of this chapter, the following terms shall have the meanings expressed below, save when the context clearly indicates otherwise:

(a) dealer: person actually interested in a dealer's contract because of his having effectively in his charge in Puerto Rico the distribution, agency, concession or representation of a given merchandise or service;

(b) dealer's contract: relationship established between a dealer and a principal or grantor whereby and irrespectively of the manner in which the parties may call, characterize or execute such relationship, the former actually and effectively takes charge of the distribution of a merchandise, or of the rendering of a service, by concession or franchise, on the market of Puerto Rico.

(c) principal or grantor: person who executes a dealer's contract with a dealer;

(d) just cause: nonperformance of any of the essential obligations of the dealer's contract, on the part of the dealer, or any action or omission on his part that adversely and substantially affects the interests of the principal or grantor in promoting the marketing or distribution of the merchandise or service.—June 24, 1964, No. 75, p. 231, § 1, eff. June 24, 1964; amended June 23, 1966, No. 105, p. 331, § 2, eff. June 23, 1966.

1966—Subsection (a): The 1966 Act amended definition of dealer so as to include not only the person so designated but also any person actually interested in a dealer's contract who acts as such.

Subsection (b): The 1966 Act included in definition of dealer's contract any contract whereby one of the parties actually acts as such "irrespectively of the manner in which the parties may call".

§ 278a. Termination of relationship

Notwithstanding the existence in a dealer's contract of a clause reserving to the parties the unilateral right to terminate the existing relationship, no principal or grantor may directly or indirectly perform any act detrimental to the established relationship or refuse to renew said contract on its normal expiration, except for just cause.—June 24, 1964, No. 75, p. 231, § 2, eff.

June 24, 1964; amended June 23, 1966, No. 105, p. 331, § 2, eff. June 23, 1966.

1966 The 1966 Act added prohibition for principal or grantor to "directly or indirectly perform any act detrimental to the established relationship".

§ 278b. Damages

If no just cause exists for the termination of the dealer's contract for detriment to the established relationship, or for the refusal to renew same, the principal shall have executed a tortious act against the dealer and shall indemnify it to the extent of the damages caused him, the amount of such indemnity to be fixed on the basis of the following factors:

(a) the actual value of the amount expended by the dealer in the acquisition and fitting of premises, equipment, installations, furniture and utensils, to the extent that these are not easily and reasonably useful to any other activity in which the dealer is normally engaged;

(b) the cost of the goods, parts, pieces, accessories and utensils that the dealer may have in stock, and from whose sale or exploitation he is unable to benefit;

(c) the good will of the business, or such part thereof attributable to the distribution of the merchandise or to the rendering of the pertinent services, said good will to be determined by taking into consideration the following factors:

(1) number of years the dealer has had charge of the distribution;

(2) actual volume of the distribution of the merchandise or the rendering of the pertinent services and the proportion it represents in the dealer's business;

(3) proportion of the Puerto Rican market said volume represents;

(4) any other factor that may help establish equitably the amount of said good will;

(d) the amount of the profit obtained in the distribution of the merchandise or in the rendering of the services, as the case may be, during the last five years, or if less than five, five times the average of the annual profit obtained during the last years, whatever they may be.—June 24, 1964, No. 75, p. 231, § 3, eff. June 24, 1964;

amended June 28, 1965, No. 104, p. 276, eff. June 28, 1965; June 23, 1966, No. 105, p. 331, § 2, eff. June 23, 1966.

1966—The 1966 Act added reference to detriment to established relationship.

1965—The 1965 Act amended first paragraph to provide that if no just cause exists for termination of contract, principal will have committed a tortious act.

§ 278c. Waiver of provisions

The provisions of this chapter are of a public order and therefore the rights determined by such provisions cannot be waived. This chapter being of a remedial character, should, for the most effective protection of such rights, be liberally interpreted; in the adjudgment of the claims that may arise hereunder, the courts of justice shall recognize the right in favor of whom may, effectively, have at his charge the distribution of activities, notwithstanding the corporate or contractual structures or mechanisms that the principal or grantor may have created or imposed to conceal the real nature of the relationship established.—June 24, 1964, No. 75, p. 231, § 4, eff. June 24, 1964; amended June 23, 1966, No. 105, p. 331, § 2, eff. June 23, 1966.

1966—The 1966 Act added second sentence relating to liberal interpretation.

§ 278d. Prescription of actions

Every action arising from this chapter shall prescribe in three years reckoning from the date of the definite termination of the dealer's contract, or of the performing of the detrimental acts, as the case may be.—June 24, 1964, No. 75, p. 231, § 5, eff. June 24, 1964; amended June 23, 1966, No. 105, p. 331, § 2, eff. June 23, 1966.

1966—The 1966 Act added words "or of the performing of the detrimental acts, as the case may be".